VER

VALTION ELÄKERAHASTO
STATENS PENSIONSFOND
THE STATE PENSION FUND

ANNUAL REPORT 2012

Contents

Balancer of pension expenditure

The State Pension Fund (VER)

The State Pension Fund (VER) is a fund external to the State budget, established in 1990, whose proceeds the Finnish state uses to prepare for the financing of future pension liabilities and the balancing of pension costs. VER is an investment organisation with the task of managing and investing the assets allocated to it by the state. The market value of VER's investment portfolio was EUR 15.4 billion at the end of 2012.

Employers and employees covered by the State Pension Scheme make pension contributions to VER. All state pensions are paid out from appropriations made for that purpose in the national budget. The execution of the state pension scheme has gradually been shifted from the State Treasury to Keva.

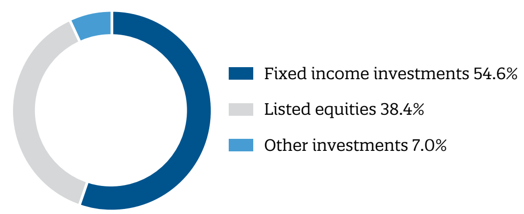
Mission

VER manages the assets entrusted to it for the long term, ensuring that its investments are secure, deliver a high return, can be converted into cash, and are appropriately diversified and spread.

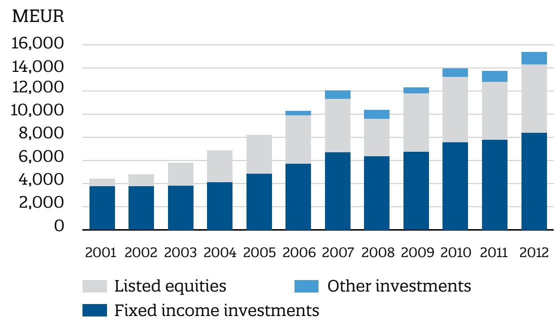
Vision

VER is a respected and successful pension investor, emphasising outstanding professional skills and ethics in all aspects of its operations.

Distribution of VER's investment portfolio on 31 Dec 2012



Development of VER's investments 2001–2012



VER 2008–2012

	2008	2009	2010	2011	2012
Total investments (MEUR)	10,359	12,318	13,937	13,736	15,359
Fixed-income investments (MEUR)	6,400	6,765	7,574	7,781	8,380
Fixed-income investments (%)	62%	55%	54%	57%	55%
Listed equity investments (MEUR)	3,183	5,024	5,632	5,006	5,899
Listed equity investments (%)	31%	41%	40%	36%	38%
Other investments (MEUR)	777	529	731	948	1,080
Other investments (%)	7%	4%	5%	7%	7%
Income from investment operations (%)					
Return on investments	-15.8	16.4	11.7	-2.3	11.3
Fixed-income investments	4.4	8.0	3.9	4.1	8.8
Listed equity investments	-42.8	38.7	23.6	-12.3	16.8
Other investments	-11.2	-14.7	8.6	6.1	3.5
Cost of investment operations (% of average capital)	0.04	0.05	0.05	0.05	0.05
Number of personnel	18	19	19	20	21
Income from pension contributions (MEUR)	1,597	1,640	1,622	1,614	1,639
Net premiums (MEUR)	271	216	154	104	35
Transfer to state budget (MEUR)	1,331	1,427	1,473	1,509	1,604
Balance sheet total (MEUR)	11,503	12,049	12,763	13,087	13,676
Pension liability (MEUR)	85,600	88,400	90,600	89,700**	92,600**
Funding ratio (%)*	12%	14%	15%	15%	17%

* Investments / pension liability

** A life expectancy coefficient was first taken into account in the pension liability calculations on 31 December 2012. The calculation is made using forecasts for the development of life expectancy from the Finnish Centre for Pensions. The like-for-like liability figure for 31 December 2011 has been recalculated to account for the life expectancy coefficient. The state pension liability confirmed for 31 December 2011 in the prior financial statements was approximately EUR 92.5 billion.

Good Returns, Responsibly

2012 turned out to be a good year for pension investors. VER achieved a return on investment of 11.3 per cent. In the long term, VER has been among the top pension investors in terms of both returns and efficiency.

European financial markets calmed down

The turmoil in the European financial markets settled somewhat during 2012. An important milestone was a statement given by the President of the European Central Bank, Mario Draghi, in late July. He said the ECB would do everything that was needed to preserve the euro. After this statement, the fixed-income and stock markets developed favourably. Europe still faces tough challenges, however. Its governments have large deficits and debt is growing in many countries. We all hope that economic growth will bring a solution to the problem, but growth prospects are still low. Naturally, there are also hopes for low interests rates and a monetary policy that will stimulate economic growth.

Good long-term returns

VER has averaged annual returns of 6.0 per cent in the last decade, with a real ten-year average of 4.1 per cent. These figures place VER among the top pension organisations in Finland. We are pleased with these results. Successful investment activities are the sum of many factors: good timing, favourable economic development, the right overall allocation, suitable risk-taking, considered prudence and the ability to perform in the global financial market. These are the elements that have contributed to VER's investment outcomes.

Another significant achievement for VER has been to accomplish excess returns in the last ten years. This means that the organisation has created added value of several million euros each year. Coupled with its good overall returns, this is an excellent accomplishment.

Efficient asset management

VER's operations have also been cost-effective. VER's total expenses, including asset management costs, have stayed below 0.3 per cent of its total assets. According to external evaluators used by the Finnish Centre for Pensions, the average for the largest Finnish pension companies is around 0.49 per cent. In its internal asset management, VER managed to keep its costs as low as 0.01 per cent. Out of VER's total expenses, less than 20 per cent comprise internal operating expenses and the rest are paid to external asset managers. Naturally internal management would be the cheapest way of handling a large investment portfolio, but VER has to supplement its own competence with the best available expertise from outside.

Growing significance of responsibility

Corporate responsibility and responsible investment are increasingly important in today's society. Companies and investors focus more and more on sustainable development issues. Like many other investors, VER has recently signed the UN Principles for Responsible Investment. These principles help us to increase the transparency of our investments and to better manage the risks of investment operations. We will continue to develop and implement sustainable operating models suitable for VER. Sustainable development can be difficult to reconcile with the objective of maximising returns, but we believe that the two are not mutually exclusive.

Investments into emerging markets

In recent years VER has increased the proportion of its investments in emerging markets. They now total 15 per cent of the fixed-income investment portfolio, as much as 30 per cent of VER's investments into sovereign bonds and 17 per cent of equity investments. In increasing our investments in emerging markets we have benefited from recent equity market crises and falling stock prices. In future years the focus of the world economy will increasingly shift to the markets that are now emerging. New countries will join the strong economic growth track.

> VER has averaged annual returns of 6.0 per cent in the last decade,with a real ten-year average of 4.2 per cent.

Balancing out the state's pension expenditure

VER is an investor of state pension assets and a buffer fund with the task of preparing for future pension expenditure and balancing out pension-related costs. VER's net cash flow will become negative in 2013. This will change VER's mission from preparing for pension expenditure to actually balancing out the expenditure. Each year VER transfers an amount equal to 40 per cent of the state's pension expenditure to the state budget. Because pension expenditure is growing, the transferred amount will also increase each year. According to estimates the peak will be reached around 2030. Pensions are paid out to state pensioners through Keva, the executor of the state pension scheme.

VER had a successful year in 2012. We achieved good returns in turbulent conditions. Our operations were cost-efficient in comparison with other Finnish and international pension investors. In the long term, we have achieved good nominal and real returns, which have exceeded the state expenditure levels. I would like to thank our competent and committed personnel and our many important stakeholders for the past year's success.

Timo Löyttyniemi
Managing Director
State Pension Fund

VER: Key Events in 2012

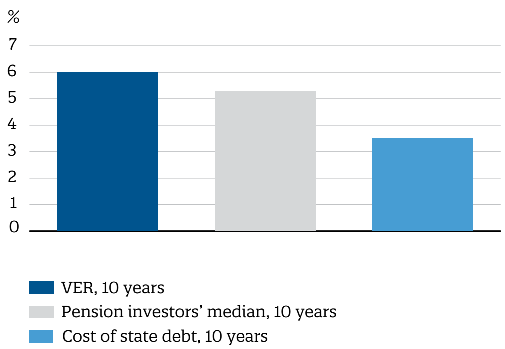
Good return on investment

- Income from investment operations: Entire portfolio 11.3 per cent, with fixed-income investments yielding 8.8, listed equity investments 16.8 and other investments 3.5 per cent.
- VER's 10-year (2003-2012) nominal return averaged 6.0 per cent per annum, and the real return averaged 4.1 per cent. In that same period, the median return for pension investors was 5.4 per cent, while the cost of the state debt averaged 3.5 per cent per annum.

VER balancing out pension expenditurer

- Total sum of pension funds held in VER by year-end 2012: EUR 15.4 billion.
- Transfer from VER to the state budget: EUR 1.6 billion, corresponding to 40 per cent of the state's annual pension costs. Transfer covered by VER's pension premium income (EUR 1.7 billion).
- From 2013, the sum of the transfer to the state budget will exceed VER's premium income. The difference will be covered by taking from VER's fund assets, which means the beginning of VER's intended duty in balancing out pension expenditure.
- The state's pension liability was EUR 92.6 billion at the year-end. The pension liability will continue to grow in the next few years, but will begin falling in the early 2020s.

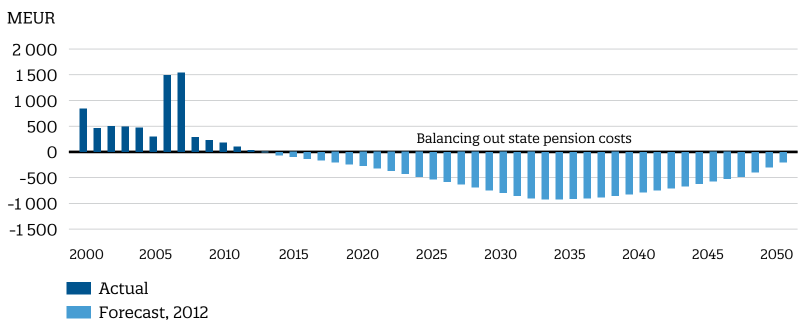
Good level of returns for VER



Pension investors' median =
median of nominal 10-year returns on investments by largest Finnish pension investors

Sources: VER, Finnish Pension Alliance investment statistics, and State Treasury

VER's net premium income



Source: State Treasury

Responsible Investment

- VER is committed to the United Nations Principles for Responsible Investment (UNPRI). VER must abide by these principles in its investment decision-making process and ownership policy, and reports on its progress annually to UNPRI.
- VER is a member of Finland's Sustainable Investment Forum (FINSIF). The purpose of FINSIF is to promote responsible investing, taking into account matters related to environment, society and corporate governance in financial management and investment decisions.

Calming down of European financial markets

- The European sovereign debt crisis subsided somewhat towards the end of the year thanks to massive financing operations from the ECB. The risk aversion of international investors also abated a little as the year progressed.

VER was one of the organisers of a meeting between Al Gore and Finnish investors in December 2012.

”Corporate responsibility and responsible investment are increasingly important in today's society. Companies and investors focus more and more on sustainable development issues.

Strengthened Confidence and Reduced Uncertainty

Global economic prospects improved during the first months of 2012.

Global economic prospects improved during the first months of 2012. The eurozone debt crisis also paused temporarily at that time. This was thanks to two massive funding operations by the ECB, in which it made available over one trillion euros in three-year loans with an interest rate of one per cent. Favourable development was boosted by simultaneous improvement of economic figures, avoidance of the immediate threat of Greek insolvency, and the approval of the second rescue package for Greece.

The favourable global market development was interrupted in the second half of March, however, as economic figures took a turn for the worse and the Spanish state economy and the banking sector were revealed to be in worse shape than expected. Figures from the United States and Asia showed a clear slowdown of economic growth in those areas.

After that, cautious indications of a re-establishment of confidence and a reduction in financial market uncertainty were observed during the year. The principal factors in this were the ECB's announcement in September of the initiation of the OMT programme, and the Federal Reserve's announcement of the third round of quantitative easing. Right at the end of the year, uncertainty grew somewhat in the US, with fierce debate over the fiscal cliff threat for early 2013.

GDP growth was zero for the the eurozone in the first quarter but turned negative over the rest of the year. The whole year's growth is estimated to have been negative by 0.5 per cent. In the United States, growth was lower than expected at the start of the year but clearly picked up after that. There, growth for the year is estimated to have reached +2.3 per cent. Out of the emerging markets, China experienced modest growth at the start of the year but also accelerated during the year. The country's growth for the whole year is estimated to have been 7.8 per cent, which is significantly slower than in previous years.

Many eurozone countries have had to tighten their fiscal policies due to growing budgetary deficits. On the other hand, the IMF has warned that tax raises will have a greater impact on growth than it was previously thought. For this reason the emphasis has shifted to ensuring the longer-term debt endurance of government finances and to laying the foundations for growth.

VER's Investment Portfolio

At the end of 2012, VER's investment portfolio had a market value of EUR 15.4 (13.7) billion. At year-end, 54.6 per cent of investments were in fixed-income instruments, 38.4 per cent in equities, and 7.0 per cent in other instruments.

The total return of the investment portfolio for 2012 was 11.3 (–2.3) per cent. The return is calculated in accordance with the recommendations of FIN-FSA and the Finnish Pension Alliance (TELA) as money-weighted return, with the cost of investment operations totalling EUR 7.1 (6.2) million.

Cautious indications of a re-establishment of confidence and a reduction in financial market uncertainty were observed during the year.

Risk Management

The identification, assessment, limitation, and control of risks are key factors in investment operations. It is the task of risk management to ensure that any realised risks do not cause substantial financial losses, endanger the continuity of operations, or weaken the confidence of stakeholders.

The comprehensive risk management plan applied by VER specifies the most important risks, risk management objectives and measures, the limits of risk exposure, responsibilities, indicators, and control principles. In setting of the limits for risk exposure, VER's risk-taking and risk-bearing capacity are taken into account. The risk management plan also takes into consideration outsourced operations.

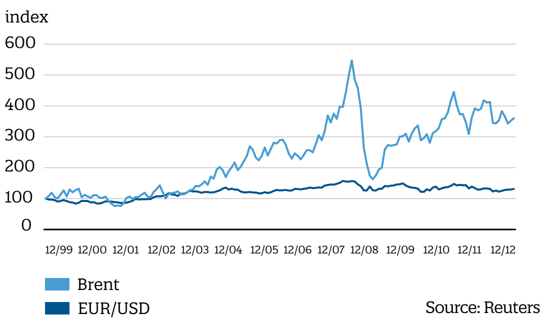
Risk surveys have been carried out jointly with PwC Finland.

VER sensitivity analysis, 31 December 2012

31 December 2012	Decline in share prices -20%	Change in interest rate +1% pt.
Capital (MEUR)	5,899*	8,380**
Effect on capital (MEUR)	-1,180	-388
In proportion to subportfolio	-20%	-5%
In proportion to entire capital	-8%	-3%

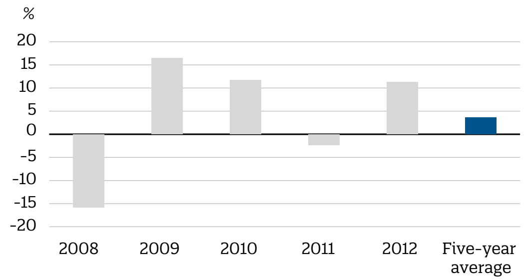
* Listed equity
** Fixed income investments

Brent and euro/dollar exchange rate development (31 Dec 1999 = 100)

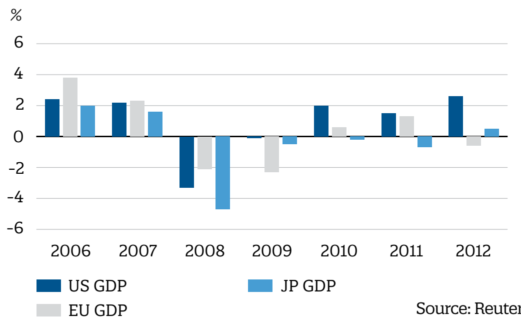


Source: Reuters

Return on VER's investment portfolio

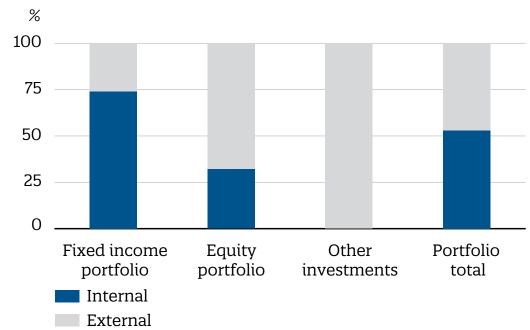


GDP development in the United States, the eurozone and Japan

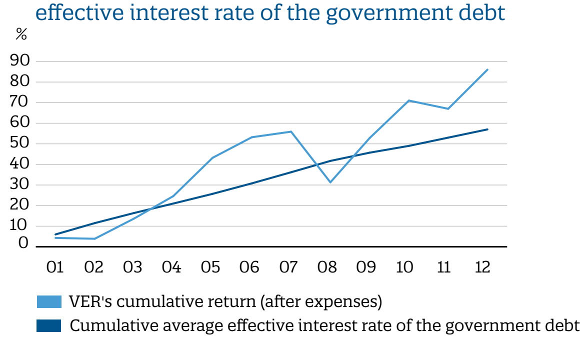


Source: Reuters

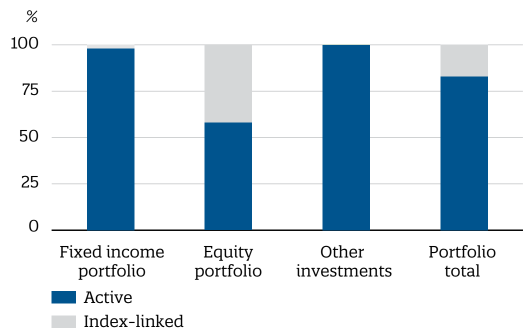
External and internal portfolio management, 31 Dec 2012



VER returns on investment vs. average effective interest rate of the government debt



Active, index-linked portfolio management, 31 Dec 2012



VER and the Fixed-Income Market

The European Central Bank stabilised the market and turned interest rates into a decline.

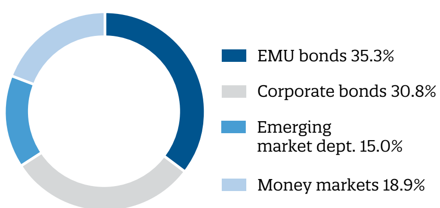
The interest rate on 10-year German government bonds fluctuated during the year following economic trends and market uncertainty. At its highest it was at 2.05 per cent and at its lowest at 1.17 per cent. Short-term interest rates (on deposits under 12 months) fell. This was due to stabilisation measures by the ECB, which significantly increased market liquidity. The funds offered to banks by the ECB were used especially for buying Spanish and Italian government bonds, substantially reducing those countries' interest rates at the start of the year. The effect was seen particularly in short-term rates. This favourable development halted in mid-March, however, when the interest rate spread between German government bonds and non-core countries bonds began growing and continued doing so until the end of June.

Returns on the fixed-income portfolio remained good, despite the low interest rates. The high credit risk market produced good returns, with the best gains coming from high yield loans and emerging market debt.

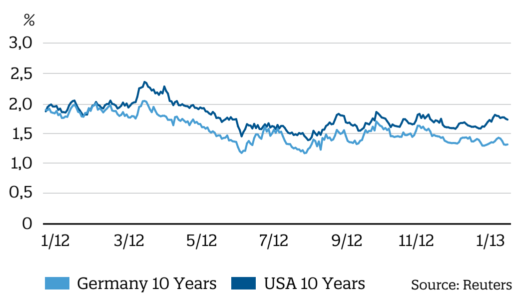
The allocation of the fixed-income portfolio was moderately adjusted during the period, with the aim of keeping the risk level low. The share of money markets and corporate bonds was over-weighted in the allocation during the year, while sovereign bonds were correspondingly under-weighted. The duration of the fixed-income portfolio was actively modified to correspond to market trends, and at the end of the year the duration was under-weighted in relation to the benchmark index.

At the year-end, VER's fixed-income portfolio amounted to EUR 8.4 billion. The return on the portfolio was 8.8 per cent in 2012. Bonds were bought and sold for a total of EUR 7.59 billion during the year 2012, while money market investments totalled EUR 2.35 billion in the corresponding period.

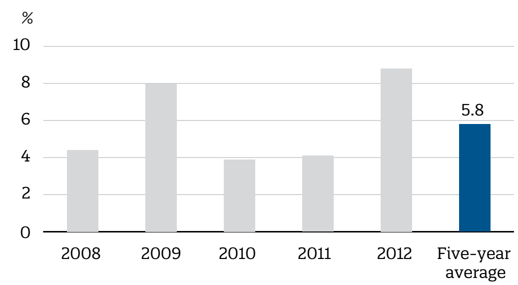
Fixed-income investments by sector 31 Dec 2012



Interest rates



Return on fixed-income investments



Good Returns from the Equity Market

2012 turned out to be a very good year for equity investors, even though major fluctuations were once again seen on the world's equity markets.

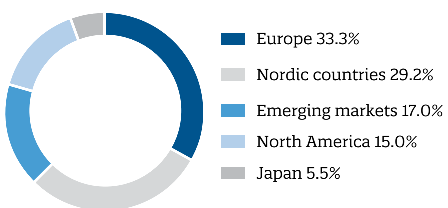
The year began with widespread equity market rises, but this was interrupted in mid-March when international investors again became worried about the state of southern European countries, especially Spain. In April and May, equity markets fell significantly all around the world. The decline evened out during the summer, when stabilisation measures taken by European governments and the ECB gradually managed to re-establish market confidence. Investor interest in higher-risk investments such as shares increased, and the second half of 2012 turned out to be very favourable for equity investors.

Returns on VER's equity portfolio, comprising listed shares and fund units, were clearly positive in 2012 at 16.8 (-12.3) per cent. The highest returns came from investments into emerging markets at nearly 20 per cent, but investments in Europe, including the Nordic countries, also yielded well. The lowest returns came from the Japanese equity market, although even those were clearly positive.

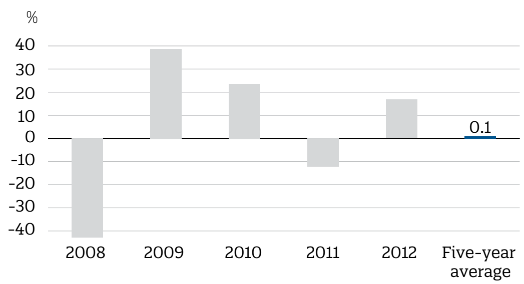
VER's net purchases of shares in 2012 totalled some EUR 57 million. VER increased the weighting of shares in its portfolio in the second quarter but correspondingly reduced it somewhat in the third quarter. Equity accounted for 38.4 per cent of the overall portfolio at year-end.

The equity portfolio's risk level corresponded to the general market in 2012, with a beta value of 1.02. At the end of the year, 68 per cent of VER's equity portfolio was invested through funds and 32 per cent was in direct investments. At that time, VER had direct equity investments in 154 companies and holdings in 60 funds.

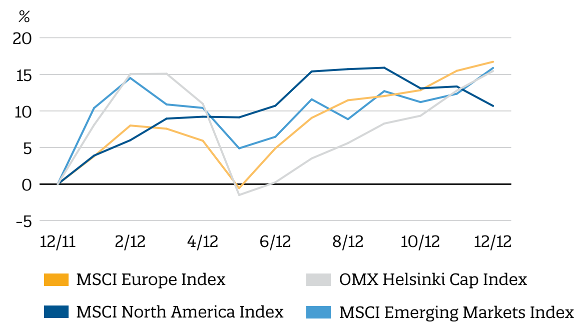
Geographic distribution of the equity portfolio 31 Dec 2012



Return on equity investments



Equity market developments in 2012



Source: Bloomberg

Fair returns in a challenging market

2012 was a relatively good year for VER's other investments, even though the market was at times subject to high uncertainty.

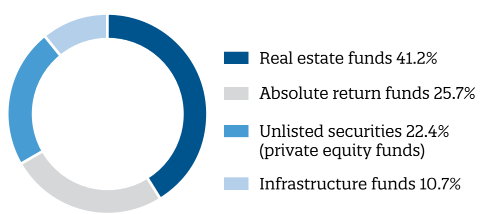
The positive development of the equity market continued almost throughout the year and this was reflected particularly in private equity fund returns. In the property market the mood remained pessimistic and property values hardly rose at all, so fund returns were modest. The polarisation of the market continued throughout the year, as investors focused on large cities and, within them, on the best properties.

For absolute return funds it was a diversified year, with severe fluctuation between returns from different strategies. The best success in 2012 was enjoyed by various credit strategies, while the lowest returns came from quantitatively modelled CTA funds. Infrastructure funds benefited from the market uncertainty, as investors focused on stable investment targets, such as public infrastructure projects.

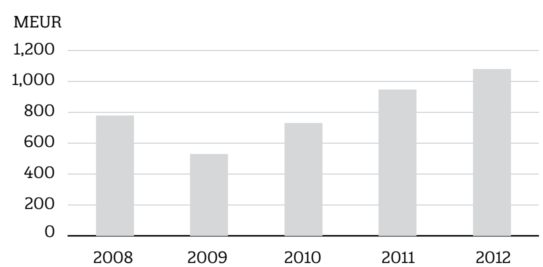
VER's 'other investments' consist of investments in real estate, private equity, infrastructure and absolute return funds. At the end of 2012, these other investments made up 7.0 per cent of VER's overall portfolio, the neutral allocation being 8 per cent. The market value of the portfolio was EUR 1,080.2 million (EUR 948.3 million). The amount of unfunded investment commitments was EUR 466.8 (339.7) million. Of total invested assets, indirect real estate investments accounted for 39.7 (42.7) per cent and listed real-estate investments for 1.5 (1.2) per cent. Private equity fund investments accounted for 22.4 (22.9) per cent, infrastructure funds for 10.7 (12.0) per cent, and absolute return funds for 25.7 (21.3) per cent of invested assets. Investments were made into 12 new funds during the year.

VER's other investments yielded a total return of 3.5 (6.1) per cent. The return on private equity investments was 7.6 (11.7) per cent, infrastructure investments 6.1 (8.8), real estate 0.1 (5.8) per cent and absolute return funds 5.7 (–0.6) per cent.

Distribution of other investments 31 Dec 2012



Market value of other investments, 2008–2012



General Investment Principles

Funding Target

According to the State Pension Act, VER's funding target is 25 per cent of the state's pension liability. VER is to accumulate assets until this target is met. At the end of 2012, the fund's market value was EUR 15.4 (13.7) billion, making the funding ratio 17 (15) per cent. Reaching of the funding target is affected by investment income, pension contribution income, and transfers to the state budget.

Principles Governing Investments

In its investment activities, VER must ensure that its investments are secure, deliver a high return, can be converted into cash, and are appropriately diversified. Investments have been diversified in a manner similar to that applied in other employment pension schemes.

VER as a Buffer Fund

State pensions in Finland are paid out from appropriations reserved in the national budget. Instead of paying out pensions, VER transfers an amount equivalent to 40 per cent of the state's annual pension costs to the state budget. The remaining assets are left in the fund. As a so-called buffer fund, VER – unlike TyEL (EPA) pension companies – does not have any pension liabilities to cover individually. Therefore, VER is not subject to regulations governing solvency.

As a long-term investor, VER makes investment decisions on the basis of its required return and the yield potential of prospective investments, taking risk levels into account. Risks are diversified through investment in various categories, markets, industries, instruments, and companies, as well as in bonds issued by different governments and of different maturities. The fund may buy or sell interest-rate and equity instruments. The real-estate, private-equity, infrastructure, and absolute return funds classed as 'other investments' are of a longer-term nature.

Fixed-income portfolio benchmark indices:	
Euro Government Composite Index	35.0%
BarCap Euro Government Inflation-Linked Bond Index	5.0%
BarCap Euro Aggregate Ex Treasury Index	30.0%
JP Morgan EMBI Global Diversified Eur Hedged	7.5%
JP Morgan GBI-EM Diversified EUR Unhedged	7.5%
JP Morgan Cash Index 3 Month	15.0%
	100.0%

Quoted equity portfolio benchmark indices:	
OMX Helsinki Cap Index	21.0%
OMX Stockholm Benchmark Cap Index	9.0%
MSCI Europe Index	26.0%
MSCI Europe Value Index	6.5%
MSCI North America Index	15.0%
MSCI Japan Index	7.5%
MSCI Emerging Markets Index	10.0%
MSCI AC Far East Ex Japan Index	5.0%
	100.0%

Other investments' benchmark indices:	
INREV Index	51.25%
Finnish Pension Alliance (pl. VER) median	26.75%
HFRI FoF Composite Index	22.00%
	100.0%

The return and profit targets set for the fund in the operation guidelines issued by the Ministry of Finance are as follows:

1. Long-term target return

In the long term, VER's investment activities must produce a higher return than an investment alternative that would be risk-free from the state's point of view. 'Risk-free alternative' refers to the cost of the state's net debt, including the cost of derivative contracts made as part of debt management. Here, 'net debt' refers to the difference between the state's budgeted debt and cash reserves.

2. Operational target return

The return on VER's investment activities, when adjusted for risk, must exceed the return of the benchmark index specified in the fund's investment plan.

Risk Limit and Strategic Allocation

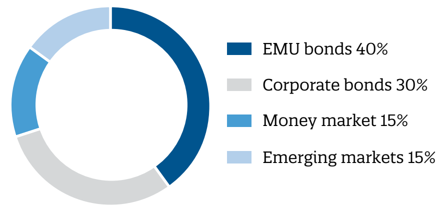
The risk limits set by the operation guidelines issued on 13 November 2007 by the Ministry of Finance are as follows:

- fixed-income investments must account for at least 45 per cent of the investment portfolio
- equity investments may not exceed 45 per cent
- other investments may not exceed 12 per cent

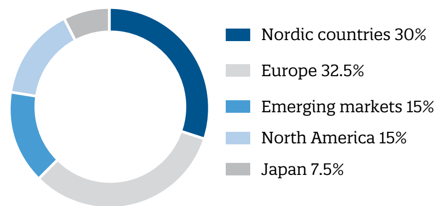
VER's annual investment plan defines a strategic allocation for the investment portfolio. The goal is to create a portfolio that yields the best possible return in the long run, at the risk level set by the Board. The strategic allocation is continuously monitored, and it can be adjusted in accordance with market changes by Board decision, within the given risk limits. Changes to the strategic allocation reflect adjustments to the fund's investment strategy.

An expected return is calculated for the portfolio annually, based on the prevailing interest rates and the risk premiums for different asset categories. The portfolio's long-term expected return in accordance with the strategic allocation is 5.6 per cent. The portfolio's expected risk level is also revised each year on the basis of the various asset categories' volatility and correlations.

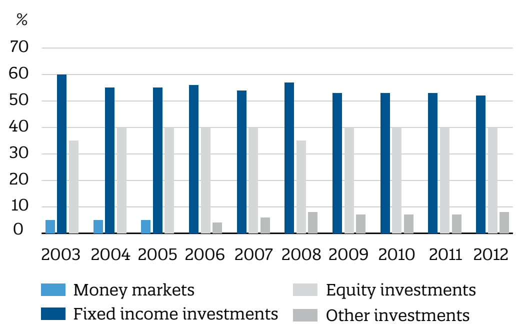
Strategic allocation of fixed-income investments at year-end 2012



Strategic allocation of equity investments at year-end 2012



Strategic allocation of VER's portfolio



Cooperation

The goal of VER is to be a respected and successful pension investor, emphasising outstanding professional skills and ethics throughout its operations. To this end, VER not only conducts successful investment activities but also cooperates with various stakeholder groups. For these purposes, VER actively networks with the management of companies in which it invests, public authorities, Finnish and foreign providers of investor and brokerage services, and other European pension investors.

Overall Assessment of Operations

The success of investment activities is analysed on a long-term basis, chiefly via consideration of the portfolio from a broad perspective. The performance of fixed-income and equity portfolios, as well as other investment portfolios, is monitored separately. Relative returns are assessed through comparison of returns with benchmark indices listed in the investment plan. If necessary, VER may liquidate losses from its investments, should the prospects for a certain investment suddenly change.

The international GIPS standards are applied in the calculation of the fund's returns. This harmonises the various methods of return and risk calculation and renders the figures comparable. Clarity and transparency are emphasised throughout the fund's operations. The responsibilities and roles of personnel responsible for investment activities are clearly defined, improving the controllability of investment activities.

VER'S INVESTMENT BELIEFS

The investment operations of the State Pension Fund (VER) have always been based on a certain number of beliefs concerning the investment market, the investment process and the organisation of investment activities. These beliefs may and do change over time, so they are periodically revised. Having these common beliefs makes it simpler to make investment decisions and directs VER's operations towards profitable investments that produce added value.

Investment beliefs in the autumn of 2012:

1. Utilising risk premiums enables strategic success.
2. Diversification reduces portfolio fluctuation.
3. Markets are for the most part effective.
4. Long-term investment offers clear benefits.
5. Excess returns come from multiple sources.
6. Organising investments is based on cost-efficiency and utilising our own strengths.
7. Professional personnel and successful selection of outside managers enable success.
8. Operations and investment beliefs are under constant review.

Responsible investment

VER does its best to observe the aims of responsible investing in its operations. For VER, responsibility means considering the environmental and social impact and corporate governance of the investment targets when making investment decisions and managing existing ones.

VER must ensure that its investments are secure, deliver returns, can be converted into cash, and are appropriately diversified. These objectives also apply to non-financial factors; in other words, VER may not invest in targets that deliver poor performance or security within the scope of corporate responsibility.

VER is a member of Finland's Sustainable Investment Forum (FINSIF). This is the Finnish contact organisation for the Principles for Responsible Investment (PRI), and its mission is to promote awareness of responsibility within financial management and investment-related decision-making.

VER has signed the United Nations PRI, committing to abiding by them in its investment operations. In the case of new investments, compliance with the principles is ensured already at the time of preparing for the investment decision. For existing investments, it takes place by monitoring investments and corporate events, and, if necessary, influencing investment targets or, ultimately, excluding the investment. The UNPRI require annual reporting from members concerning implementation and compliance.

In addition, VER complies with the recommendations for investment operations of the Finnish Pension Alliance (TELA), whose principles for responsible investment are based on sustainable development, the United Nations Global Compact, and the UNPRI.

VER's Shareholder Policy

According to its shareholder policy, VER operates as an independent portfolio investor. The fund is a long-term investor and major shareholder in a number of companies. The companies must ensure the increasing value of their shares in the long term.

VER can best promote the successful performance of its portfolio companies by following up on it. In 2012, VER attended the AGMs of 14 Finnish companies. By attending AGMs and exercising its voting rights, VER can influence decisions that are significant in terms of the companies and their shareholders.

No VER personnel are involved in the management of listed companies in which they have holdings.

RESPONSIBLE INVESTMENT

For VER, responsible investment implies effective and consistent observance of the investor's responsibility. It encompasses monitoring the responsibility and sustainable development of target companies, as well as conducting responsibility-related dialogue with these and with external asset managers.

The principles of responsible investment apply to all fixed-income, equity and alternative investments made by VER. Their implementation may vary by the type of investment, however, as their applicability differs in the various categories.

In its responsible investment operations, VER observes the following principles of ethical and sustainable development:

- Ethical investment refers to avoiding certain industries (companies whose revenues comprise significant portions coming from arms, alcohol, tobacco, gambling or adult entertainment).
- Sustainable investment refers to considering ESG (environmental, social and governance) factors in the investment process.

Criteria and their Application

The ethical principles are applied in all direct investments.

The sustainable development principles are applied by using ESG criteria in evaluating investment targets.

The ethical and ESG factors are included in the investment decisions. VER is aware of the fact that these principles may be difficult to abide by in the case of certain complex investment instruments.

The fulfilment of responsibility principles is evaluated regularly and action is taken where necessary. External asset managers are also expected to take into account ESG factors, and the extent to which they do is periodically assessed.

Application of principles

- Evaluation of ethicalness and sustainability
- Assessment of external asset managers
- Dialogue with target companies and external asset managers
- Influencing methods
- Annual reporting

VER's Board of Directors receives reports on the fulfilment of responsible investment principles in VER's operations.

The State Pension Security

In 2012, the Finnish State Pension Act covered more than 155,000 people, of whom some 83,000 were state employees.

The state's pension expenditure was EUR 4.0 billion, i.e. over 18 per cent of all employment pensions. There were around 360,000 state pensioners, corresponding to over 26 per cent of all employment pension recipients.

The State Pension Scheme as part of the Finnish Employment Pension Scheme

After a pension reform in 2005, state pension cover, originally slightly better than the cover under the Employees Pensions Act, is on a par with the local government and private sectors. The reform also introduced a career model for state pensions, where pensions are calculated on the basis of annual earnings and a growth percentage. A pension is accumulated for work done between the ages of 18 and 68, and an increased growth percentage, known as super-accumulation, encourages 63-year-olds to continue working. Integration of pensions was abolished, which means that the maximum pension accumulation limit of 60–66 per cent no longer exists. The pension reform also means that a life expectancy coefficient, used to prepare for longer life expectancy, affects the amount of pensions.

State Pension Security

Since the beginning of 2011, execution of the state pension scheme has been the task of Keva (formerly the Local Government Pensions Institution). From 2013, also duties related to employers and actuarial services will be transferred to Keva from the State Treasury.

State pensions are paid out from appropriations reserved for the purpose in the State budget. The State is responsible for ensuring that accrued pensions can be paid in the future. In the state pension system, the employers and employees pay the sum equivalent to the amount accrued in pensions each year as pension insurance premiums to VER. The state is aiming at a 25 per cent funding ratio in proportion to pension liability.

Balancing the Financing of Pension Costs

Through the State Pension Fund, the state prepares for financing pensions payable in the future, and especially to even out the coming pension costs of the baby boom generation.

Some of VER's assets are transferred to the state budget each year. The transfer is justified in that all state pensions are paid out from budget appropriations, and therefore some of the pension fund's assets can be used for the payment of pensions. The transfer of funds to the state budget has been a crucial factor in regulating VER's growth. The State Pension Act specifies the transferable amount, which is 40 per cent of annual state pension expenditure. By the end of 2012, a total of EUR 21 billion in VER assets had been transferred to the state budget. By parliamentary decision the transfers of VER assets to the state budget were substantially reduced in 2006 and 2007 in order to allow a greater expansion of the State Pension Fund.

In 2012, the pension premium income still exceeded the sum transferred from VER to the state budget. From 2013, the budget transfer will exceed premium income, which means that VER will begin to fulfil its originally intended task of balancing out pension expenditure. If the present funding mechanism continues, the state pension scheme's pension contribution cost, meaning the net cash flow tied into the state pension scheme each year, will long remain lower than the actual pension expenditure.

Supervision of VER

VER is supervised by the Financial Markets Department of the Finnish Ministry of Finance. VER's investment activities are directed by the Board of Directors, appointed by the Ministry of Finance, which includes representatives from both the employers and the employees. VER manages the assets entrusted to it and makes all investment decisions in accordance with the investment plan adopted by the Board of Directors, and within its investment authorisations and set limits.

Pension Costs in Relation to Payroll

The proportion of the state's pension expenditure in relation to state payroll will continue growing sharply until the beginning of the 2030s. In 2012, the proportion of pension expenditure in the payroll was approximately 60 per cent; it is expected to peak in 2031 at over 85 per cent. After this peak, the proportion will slowly fall until the end of the 2040s. After the mid-2070s, pension expenditure is expected to stabilise at around 34 per cent of payroll.

Calculated in euros (at the 2012 value), pension expenditure will peak in 2032 at approximately EUR 5.1 billion. The number of employees covered by the state pension scheme (VaEL) is expected to fall sharply by the mid-2040s, which will also reduce pension expenditure.

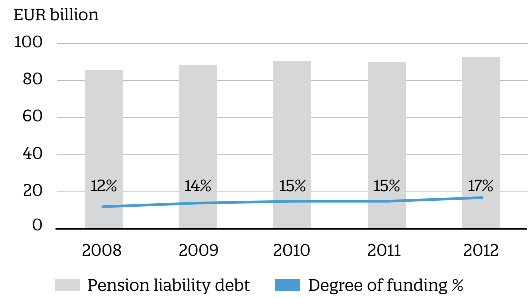
In recent years, the new Universities Act has had a particular impact on the number of VaEL employees, as only staff born before 1980 remain within the scope of the state pension scheme since 2010. With the reform, in 2010 the number of university employees covered by VaEL was reduced by 8,700, and it will continue to decrease until Finnish universities no longer employ anyone covered by the state pension scheme. The impact of the Universities Act will not become significantly visible as a saving in state pension expenditure until the mid-2040s. However, as the state payroll decreased, VER's pension contribution income was reduced already in 2010. The pension contribution income of VER is reduced by a reduction in VaEL payroll in universities, local governments and state-subsidised institutes, and by lower growth in the state pay arising from the government productivity programme. According to an estimate by the State Treasury, the growth of VER's pension contribution income will continue to slow down until the late 2040s, after which it will achieve steady growth according to the earnings index.

State Pension Liability

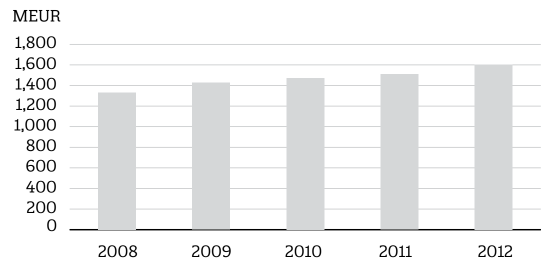
Pension liability refers to the sum of money and its future return on investment which, calculated at a certain point in time, would cover the future pensions earned by the time of calculation. The liability includes all paid-up pensions (pensions deriving from finished state employment relationships), also for former state employees who have become employees of local governments or private companies or have left state employment due to incorporation of state institutions. Therefore, pension liability always involves an assumption regarding return on investment. The state's pension liability indicates the cost of the pensions promised by the state to its current and previous employees, at the time of calculation.

In addition to expected returns, the pension liability calculation includes other assumptions related, for instance, to changes in life expectancy and retirement age, and to how many people are expected to take disability pensions in the future. To calculate pension liability, it is essential to know the accurate sum of pensions accrued until the time of calculation. Because the employed population accumulates a pension each year, new people retire, and people entitled to receive pensions die, the pension liability sum is not constant but is recalculated annually.

Pension liability debt and degree of funding



Asset transfer from VER to the state budget



The pension liability figure consists of provisions for earned premiums and unearned premiums. The former refers to the amounts to be paid to people who have already retired – i.e., the capital value of old-age, family, disability, unemployment, and part-time pensions that have already started being paid out. The latter refers to the capital value of pensions accrued by the time of calculation that have not yet begun to be paid out.

Calculation of Pension Liability

For the purposes of the financial statements of the state and of the State Pension Fund, Keva (formerly the Local Government Pensions Institution) calculates the pension liability according to the full funding principle, following (where applicable) the calculation instructions provided for pension funds by the Financial Supervisory Authority, the calculation principles concerning registered supplementary pension benefits set forth in the Employees Pensions Act, and the provisions of the State Pension Act. The basis lies in mathematical models and calculation principles generally accepted in the insurance field.

Pension liability is calculated individually up until the end of the calendar year preceding the financial year, for every person who has, at some point in his or her employment history, accrued a Finnish state pension, whether retired, employed under the State Pension Act, or no longer employed but not yet retired. The calculation is done according to the so-called prospective method, in which the capital value of pensions accrued to date under the State Pension Act is calculated by discounting pensions to be paid in the future to their current value.

The calculation uses the mortality and incapacity pension statistics of the TyEL basic employee pension scheme. The discount rate used is 2.7 per cent, which is considered to be a real rate of interest that will exceed future income level changes and index increases in pensions. From 2012 onwards, the pension liability calculation also takes into account a life expectancy coefficient drawn from estimates concerning life expectancy development from the Finnish Centre for Pensions.

The liability for the rest of the financial year is calculated retrospectively from the previous year's liability by adding the new liability generated during the year (pension premium income) and deducting the realised liability (pension cost), taking into account interest.

State pension liability, 2012

Year	Pension liability	Pension liability without life expectancy coefficient
2012	92.6	94.8

State pension liability, 2009-2011

Year	Pension liability	Pension liability without life expectancy coefficient
2011	89.7	91.6
2010	88.6	90.4
2009	87.4	89.1

The comparison data for 2009–2011 were recalculated using updated register figures and the latest life expectancy coefficient forecast from the Finnish Centre for Pensions.

Pension liability according to IFRS

Year	Pension liability
2012	151
2011	120

At the year-end 2012, the state pension system's pension liability was EUR 92.6 billion (like-for-like pension liability for year-end 2011, adjusted with the life expectancy coefficient, was EUR 89.7 billion). While the state's pension liability is expected to grow in real terms in coming years, it will begin to decline in the early 2020s and continue to do so until the mid-2050s. This decline will be due to the decreasing proportion of accumulated pensions thanks to increases in total salaries, and to the fact that, as the baby boom generation retires, the current pension liability will begin to be defused in the form of paid-out pensions.

Calculated according to IFRS, the state's pension liability at the year-end was EUR 151 billion (EUR 120 billion in 2011). In the IFRS calculation, pension liability is affected by the chosen discount rate and its fluctuation. The discount rate used was the nominal interest rate on 20-year AA-rated corporate bonds, which was 2.824 per cent on 31 December 2012 (3.684).

PENSION LIABILITY

What is pension liability?

Pension liability refers to the sum of money and its future return on investment that, calculated at a certain point in time, would cover the future pensions earned at the time of calculation. Therefore, pension liability always involves an assumption regarding the return on investments. The state's pension liability indicates the cost of the pensions promised by the state to its current and previous employees, at the time of calculation.

In addition to expected returns, the pension liability calculation includes other selected assumptions related, for instance, to changes in life expectancy and retirement age, and to how many people are expected to take disability pensions in the future.

To calculate pension liability, it is essential to know the accurate sum of pensions accrued until the time of calculation. Because the employed population accrue pensions each year, new people retire, and people entitled to receive pensions die, the pension liability sum is not constant but is recalculated annually.

What makes the state's pension liability sum so large?

According to the the estimated value of accumulated employee pension was EUR 623.4 billion with 2.5% real interest rate on 31 December 2010 (5/2011 report by the Finnish Centre for Pensions Statutory pensions. Long-term projections 2011. Ismo Risku, Kalle Elo, Tapio Klaavo, Sergei Lahti, Hannu Sivonen ja Risto Vaittinen).

What is the role of VER?

External to the State budget, the State Pension Fund is responsible for investing the state's pension assets. The State Pension Fund was founded as a buffer fund to balance the effects of state pension expenditure to the national economy. In particular, the purpose of funding was to prepare for the retirement of the baby boomers and the increasing pension expenditure.

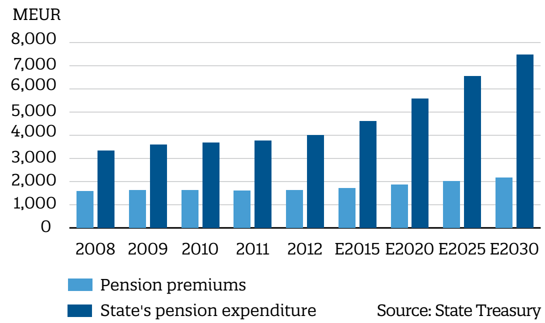
What is the degree of funding in pension liability?

= VER's assets on 31 December 2012 / MEUR 92,600. The degree of funding is 17 per cent.

In the end, who is responsible for pensions?

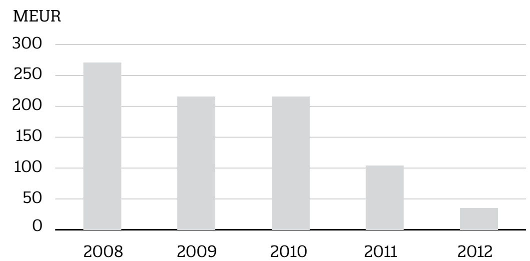
The State's pension expenditure belongs to statutory expenses and therefore defrayed by the State. Employment pension institutions are (jointly) responsible for the employee pensions (TyEL).

VER's pension premiums and the state's pension expenditure



Source: State Treasury

VER's net premiums, five years



VER's Organisation

Board of Directors, 1 March 2012 – 28 February 2015

Chairman
Antti Tanskanen
born 1946
Education: Doctor of Economics

Vice Chairman
Professor
Hannu Kahra
University of Oulu
born 1950
Education: Doctor of Philosophy

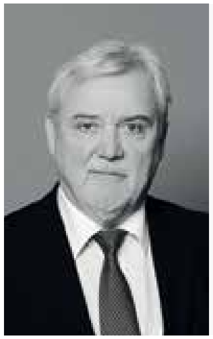
Personal Deputy Manager
Financial Adviser
Asko Lindqvist
Ministry of Finance
born 1952
Education: Master of Science (Economics and Business Administration)

Professor
Minna Martikainen
Aalto University's School of Economics
born 1969
Education: Doctor of Economics

Personal Deputy Manager
Financial Adviser
Mika Kuismanen
Ministry of Finance
born 1967
Education: Ph.D

Director of the Administrative Governance and Development
Helena Tarkka
Ministry of Finance
born 1955
Education: Master of Political Science, Associate of Laws

Personal Deputy Manager
Senior Financial Adviser
Pauli Kariniemi
Ministry of Finance
born 1970
Education: Master of Science (Economics and Business Administration)



Director of Negotiations
Risto Kangas
JUKO Trade Union
born 1954
Education:
Comprehensive-school teacher

Personal Deputy Manager
Negotiations Manager
Markku Nieminen
JUKO Trade Union
born 1953
Education: Bachelor of Laws

Chairman
Antti Palola,
Federation of Salaried Employees Pardia
born 1959
Education: Sea captain

Personal Deputy Manager
Administrative Manager
Anne Puolakka
Federation of Salaried Employees Pardia
born 1955
Education: Vocational Qualification in Business and Administration

Administration Manager
Pirjo Mäkinen
The Trade Union for the Public and Welfare Sectors (JHL)
born 1955
Education: Master of Science

Personal Deputy Manager
Legal Affairs Manager
Mika Hämäläinen
The Trade Union for the Public and Welfare Sectors (JHL)
born 1959
Education: Bachelor of Laws

Investment Consultative Committee, 31 December 2012

Chairman
Eva Liljeblom, Rector of Hanken School of Economics

Vice-Chairman
Vesa Puttonen, Professor, Aalto University

Topi Piela, Managing Director of Umo Capital Oy

Timo Hukka, Investment Director, Suomi Mutual Life Assurance Company

Liisa Jauri, Director, Nordea

Erik Valtonen, PhD

Hanna Kaleva, Managing Director, Institute for Real Estate Economics

The Management Team

Timo Löyttyniemi	Maarit Säynevirta	Jukka Järvinen	Seija Kettunen	Jan Lundberg	Tiina Tarma
Managing Director	*Head of Other Investments*	*Head of Fixed Income*	*Head of Administration*	*Head of Equities*	*Legal Counsel*

The State Pension Fund is administered by the Board of Directors and the managing director, assisted by a management team. The Ministry of Finance appoints the Board of Directors, which manages the fund's investments, decides on investment policies and approves the annual investment plan. The Board's term of office is three years. The Board consists of a chairman, a vice chairman and up to five other members. A personal deputy is appointed for each member.

The current Board began its term on 1 March 2012, and is chaired by Antti Tanskanen, PhD (Econ.). The Board of Directors convened 11 times in 2012. In addition to investment operations, the meetings concerned matters related to responsible investing; derivatives; changes to the premium criteria of the state pension system; and the condition of the global and, particularly, European economies.

The Board of Directors appoints a consultative committee with seven members, who are external investment and finance professionals. The Consultative Committee assesses the fund's investment plan, monitors its realisation, and reports to the Board of Directors. The Consultative Committee convened three times in 2012.

The VER management team, consisting of the managing director and five other members, convenes regularly.

The State Pension Fund

1989

- The State Pension Fund is established within the State Treasury for the purpose of preparing for future pension costs and for balancing out pension expenditure.
- The funding target, 1.5 times the state payroll as in private pension schemes, is set for 2010.

1991

- Pension contributions from state offices, institutions, and enterprises are directed to VER.

1993

- Pension contributions from state employees are directed to VER.
- Investment activities are expanded.
- The transfer of funds to the budget is restricted (to three quarters of pension expenditure).
- The VER Board of Directors is appointed to bear responsibility for the fund's investment activities.

1994

- The funding target is revised and now encompasses the whole state pension scheme instead of the former state payroll figure.
- Director General Teuvo Metsäpelto starts as the first Chairman of the Board of Directors.

1999

- Municipalities start to pay in pension contributions for teachers to VER.

2000

- The budget transfer is reduced to one third of annual pension expenditure until the end of 2006 (subsequent to this, one half).
- The funding target is revised to be 1.5 times the total state payroll in 2010 and is tied to the state's pension liability (being at least 20 per cent in 2010).
- Dedicated staff are hired for the fund.
- Investment activities are extended to include equity investments.

2003

- Eino Keinänen is appointed Chairman of the Board of Directors.
- The fund's first full-time managing director, Timo Löyttyniemi, is appointed.

2005

- The funding target is set at 25 per cent of the state's pension liability, and this is expected to be achieved by 2020.
- The annual transfer from VER to the state budget is prescribed as equalling 40 per cent of annual pension expenditure until the target funding ratio is met. Subsequently, the amount of the transfer is to be specified annually in the state budget.

2006

- The role of the Ministry of Finance as supervisor of VER is defined more precisely, and the ministry is granted the right to issue general regulations concerning VER's administration, finances and investment policies.
- The tasks of the VER Board of Directors are laid down in the law.
- The duties of VER's auditors are laid down in the law.
- The transfer of assets from VER to the state budget is reduced for 2006 and 2007 to expand the fund.
- The Ministry of Finance issues its first operating guidelines to VER in November.

2007

- The 1989 State Pension Act with all its amendments is revoked and a new Act is passed.
- In March and November, the Ministry of Finance further specifies the operating guidelines issued in 2006.

2008

- The global financial crisis begins.

2009

- Antti Tanskanen is appointed as Chairman of the Board of Directors.
- A reform of the Universities Act is implemented, which leads to the gradual transfer of university employees to private pension schemes.

2010

- VER celebrates its 20th anniversary.
- The European debt crisis begins.

2011

- European sovereign debt crisis.
- VER signs the United Nations Principles for Responsible Investment (UNPRI).
- VER joins Finland's Sustainable Investment Forum (FINSIF).
- The execution of state pension security is transferred from the State Treasury to Keva.

2012

- The sum of VER's investment assets exceeds EUR 15 billion.
- The decision is made to transfer the employer services related to the state pension scheme to Keva from the start of 2013.

VER profit and loss statement

	1 Jan–31 Dec 2012		1 Jan–31 Dec 2011	
OPERATING INCOME				
Other operating income				
Sales gains on equities and shares	135,423,651.64		108,348,895.55	
Pension contributions from State offices and institutions	741,326,330.20		738,505,999.85	
Other pension contribution income	518,998,141.01		531,723,300.54	
Employees' pension contributions	372,713,777.80		338,858,855.86	
Disability insurance contribution income	5,761,280.00	1,774,223,180.65	4,721,618.00	1,722,158,669.80
OPERATING EXPENSES				
Materials, supplies and goods				
Purchases during the period	83,145.29		55,539.99	
Personnel expenses	2,880,727.57		2,392,764.93	
Rents	267,989.64		260,477.16	
Outsourced services	3,440,633.56		3,158,566.12	
Other expenses				
Other expenses	332,255.87		315,857.69	
Sales losses on equities and shares	21,784,820.80		64,033,266.84	
Depreciation	53,211.17	-28,842,783.90	60,753.52	-70,277,226.25
SURPLUS I		1,745,380,396.75		1,651,881,443.55
FINANCIAL INCOME AND EXPENSES				
Financial income	456,811,808.10		313,146,908.28	
Financial expenses	-75,769,853.61	381,041,954.49	-160,147,691.97	152,999,216.31
SURPLUS II		2,126,422,351.24		1,804,880,659.86
INCOME AND EXPENSES FROM TRANSFERS				
Income				
Transfer fees		29,889,257.26		25,706,289.02
SURPLUS III		2,156,311,608.50		1,830,586,948.88
SURPLUS/DEFICIT FOR THE PERIOD		2,156,311,608.50		1,830,586,948.88

Balance sheet

ASSETS	31 Dec 2012		31 Dec 2011	
FIXED ASSETS AND OTHER LONG-TERM INVESTMENTS				
INTANGIBLE ASSETS				
Other long-term expenditure		30,398.30		58,458.32
TANGIBLE ASSETS				
Furniture and fittings	31,670.90	31,670.90	44,001.63	44,001.63
SECURITIES HELD AS FIXED ASSETS AND OTHER LONG-TERM INVESTMENTS				
Purchases of bonds denominated in euros	4,283,992,357.61		4,757,545,468.61	
Other long-term investments denominated in euros	5,401,893,875.24		4,784,081,111.44	
Purchases of bonds denominated in foreign currencies	257,431,778.81		0.00	
Other long-term investments denominated in foreign currency	2,213,811,960.63	12,157,129,972.29	2,118,497,110.61	11,660,123,690.66
TOTAL FIXED ASSETS AND OTHER LONG-TERM INVESTMENTS		12,157,192,041.49		11,660,226,150.61
LONG-TERM RECEIVABLES				
Long-term receivables		27,767.68		208,577.75
CURRENT RECEIVABLES				
Accrued credits and deferred charges	213,618,490.60		219,445,711.84	
Other current receivables	21,043,717.88	234,662,208.48	14,448,579.47	233,894,291.31
FINANCIAL SECURITIES AND OTHER SHORT-TERM INVESTMENTS				
Purchases of bonds denominated in euros		959,419,668.77		940 620 089.24
CASH, BANK DEPOSITS AND OTHER FINANCIAL ASSETS				
Other bank accounts	324,255,176.85	324,255,176.85	251,824,778.40	251,824,778.40
TOTAL INVENTORIES AND FINANCIAL ASSETS		1,518,364,821.78		1,426,547,736.70
TOTAL ASSETS		13,675,556,863.27		13,086,773,887.31

EQUITY AND LIABILITIES	31 Dec 2012		31 Dec 2011	
EQUITY				
Fund capital	-19,406,903,064.37		-17,897,522,909.37	
Accrued changes in capital	32,489,879,067.17		30,659,292,118.29	
Budget transfers	-1,603,669,146.96		-1,509,380,155.00	
Surplus/deficit for the period	2,156,311,608.50	13,635,618,464.34	1,830,586,948.88	13,082,976,002.80
LIABILITIES				
CURRENT				
Accounts payable	537,051.88		554,531.47	
Items to be rendered forward	42,515.00		39,376.37	
Accrued charges and deferred credits	39,292,640.16		3,141,263.69	
Other current liabilities	66,191.89	39,938,398.93	62,712.98	3,797,884.51
TOTAL LIABILITIES		39,938,398.93		3,797,884.51
TOTAL EQUITY AND LIABILITIES		13,675,556,863.27		13,086,773,887.31

Portfolio Structure and Returns, 2001–2012

	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003	2002	2001
Structure of portfolio (at year-end)												
AUM (MEUR)*	15,359.0	13,736.1	13,937.1	12,318.0	10,359.4	12,050.9	10,305.6	8,200.6	6,867.1	5,795.0	4,840.6	4,426.9
Allocation, %	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Fixed-income investments	54.6%	56.6%	54.3%	54.9%	61.8%	55.7%	55.5%	59.1%	59.9%	65.9%	78.0%	84.8%
Listed equities	38.4%	36.4%	40.4%	40.8%	30.7%	38.0%	40.4%	39.6%	40.1%	34.1%	22.0%	15.2%
Other investments	7.0%	6.9%	5.2%	4.3%	7.5%	6.3%	4.1%	1.3%	0.0%	0.0%	0.0%	0.0%
Performance and costs, %												
Return before investment costs	11.4%	-2.3%	11.7%	16.5%	-15.7%	1.8%	7.0%	15.0%	9.6%	9.5%	-0.4%	4.3%
Fixed-income investments	8.8%	4.1%	3.9%	8.0%	4.4%	1.8%	0.1%	5.4%	7.0%	4.0%	7.2%	5.2%
Listed equities	16.8%	-12.3%	23.6%	38.7%	-42.8%	0.7%	17.4%	31.5%	14.4%	20.7%	-23.7%	-11.5%
Other investments	3.5%	6.1%	8.6%	-14.7%	-11.2%	9.5%	6.7%	2.2%	-	-	-	-
Excess return before costs**	n/a	0.6%	1.1%	-0.2%	0.0%	0.0%	-0.1%	0.2%	0.0%	0.1%	-2.4%	-0.1%
Excess return before costs (excl. other investments)	0.1%	0.4%	1.4%	0.6%	1.1%	n/a	n/a	n/a	n/a	n/a	n/a	n/a
Costs (% of average invested capital)	0.05%	0.05%	0.05%	0.05%	0.04%	0.04%	0.05%	0.05%	0.05%	0.05%	0.04%	0.02%
Return after investment costs	**11.3%**	**-2.3%**	**11.7%**	**16.4%**	**-15.8%**	**1.8%**	**7.0%**	**14.9%**	**9.6%**	**9.4%**	**-0.4%**	**4.3%**
Risk indicators												
Volatility***	5.0%	6.3%	5.0%	8.3%	10.2%	3.5%	4.1%	4.5%	3.3%	3.6%	3.7%	2.7%
Volatility (benchmark)***	5.1%	6.5%	5.0%	9.2%	11.7%	3.6%	4.0%	4.5%	3.4%	3.7%	3.3%	3.3%
Jensen's alpha***	0.4%	-0.2%	1.8%	3.2%	-0.1%	-0.2%	0.2%	1.5%	0.7%	1.1%	-2.3%	-0.2%
Tracking Error***	0.4%	0.6%	0.3%	1.3%	0.8%	0.3%	0.7%	0.5%	0.4%	0.6%	0.9%	1.0%
Beta***	1.0	0.9	1.0	0.8	0.8	0.9	0.9	0.9	0.9	0.9	1.0	0.7
Sharpe Ratio***	2.3	neg	2.2	1.9	neg	neg	1.0	2.9	2.2	1.9	neg	neg
Sharpe ratio (benchmark)***	2.2	neg	1.9	1.6	neg	neg	1.0	2.8	2.2	1.8	neg	neg
Information ratio***	0.4	0.6	4.5	0.5	1.3	-0.4	-0.1	0.5	0.0	0.3	-2.7	-0.1
Effective average interest rate on government debt**, %**	**2.3%**	**2.5 %**	**2.5 %**	**2.8%**	**4.1%**	**4.1%**	**4.1%**	**3.9%**	**3.9%**	**4.4%**	**5.2%**	**6.0%**

*) AUM corresponds to the market value of investments, plus accrued interest, investment bank account values, market values of forward contracts, warranties received and open deals. Exchange rate: ECB fixing.
**) Excess return for the whole portfolio for the financial year under review will be available in spring 2013 once the benchmark indices are ready.
***) Excluding other investments whenever a figure is available for other investments; otherwise applies to whole portfolio.
****) The effective average interest rate on government debt and the return on investment operations are calculated using different principles, so they are not directly comparable.

Cumulative return over 10 years (2003–2012)	78.7%
Average annual return over 10 years (2003–2012)	6.0%
Real return over 10 years (2003–2012)	4.1%
Average annual return over 5 years (2008–2012)	3.6%

Glossary

Absolute-return fund
A fund that applies active and unrestricted investment strategies to benefit from diverse alternative risk premia on the fixed-income, equity, foreign exchange, commodity, and credit markets. These funds have a low correlation with the equity and fixed-income markets.

Benchmark index
The index to which the returns and risks of an investment are compared.

Beta
Measurement factor for the sensitivity of an investment to fluctuations in the value of the benchmark index. If an investment's beta is less than 1, the investment is not expected to fall at the same rate as the index.

Bond
An instrument through which companies, national and local governments, and other organisations (issuers) can take out a loan from the public by issuing debenture bonds, more commonly known as bonds.

Certificate of deposit
A marketable promissory note issued by a bank.

Commercial paper
A short-term marketable promissory note issued by a company.

Correlation
Dependence between variables – for example, the relationship between different financial instruments or types of assets.

Derivative
A financial instrument whose value is based on another, underlying security, index, currency, commodity, or option.

Effective yield
The return on a security in relation to its market value.

Excess return
The difference between the returns of the portfolio and the benchmark index.

Forward contract
A contract involving the obligation to buy or sell an underlying security, such as a share, for a specified price in the future.

Funding ratio
The ratio between funded assets and pension liability.

High-yield investment fund
A registered fund that invests in bonds promising to pay higher yields on account of the low credit rating of the issuing company.

Inflation-linked bond
Primarily sovereign bonds, with interest rate and principal are adjusted in proportion to changes in the consumer price index for reaching the agreed real return between the issue date and the maturity date.

Information ratio
The ratio between a portfolio's active return and tracking error.

Investment commitment
A commitment given by a private-equity fund investor to the fund, which is fulfilled when the fund makes capital calls to raise cash for its investments.

Investment-grade fund
A corporate bond fund that invests in bonds issued by companies with high credit ratings, offering higher interest than sovereign bonds do.

Liquidity
The convertibility of an investment into cash. A liquid investment can quickly be converted into cash.

Market risk
The effect of general market movements on the price of a share, a systematic risk.

Modified duration
Sensitivity of a fixed-income investment to fluctuations in interest rates. The longer the duration, the higher the interest-rate risk.

Option
A contract involving the right to buy or sell an underlying security, such as a share, for a specified price in the future.

Pension liability
The nominal value of pensions earned by a certain point in time.

Sharpe ratio
The return on an investment, adjusted for risk, comparing the return that exceeds the risk-free return to the volatility of the return. The higher the Sharpe ratio, the better the risk-adjusted return. The risk-free return is usually estimated as the calculated return on a short-term money market investment.

Tracking error
Standard deviation of the excess return, measuring how closely the yield on an investment follows the yield of the benchmark index. A high tracking error means that the yield on the investment has fluctuated a lot in comparison to the benchmark index. The tracking error (active risk) of a passive portfolio is close to 0.

Volatility
The standard deviation of the return – the most common risk indicator. It measures the fluctuations in the return on an investment; the higher the risk, the greater the volatility. For example, a volatility figure of 20 means that if the expected return is 10 per cent, in two years out of three the return on the investment will be between -10 and +30 per cent.

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